IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

Nos 55-56

THE UNITED STATES OF AMERICA,
Petitioner,

vs.

ARNOLD W. KRUSE,
Respondent.

THE UNITED STATES OF AMERICA,
Petitioner,

vs.

LESTER A. KRUSE,
Respondent.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

PETITION FOR REHEARING.

GEORGE K. BOWDEN,
Counsel for Arnold W. Kruse and Lester A. Kruse, Defendants Respondents.

JOSEPH A. STRUETT,
WARREN CANADAY,
Of Counsel.

THE DUNTHORP-WARREN PRINTING COMPANY, 310 WEST JACKSON, CHICAGO

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The opinion of this Court, rendered January 5, 1942, clearly and succinctly outlined the facts of this case and laid down reasonable and understandable principles of law as applied to them. The legal contentions raised by our brief were fully recognized by this Court when it held that the dominant issue in this case was whether these payments were reasonable compensation. Our legal contentions were answered when this Court held as a matter

of law that the government's evidence was sufficient to establish a *prima facie* case that the commissions paid the defendants were unreasonable compensation. While we do not agree with this Court's conclusion as to the question of variance, the problem presented herein is far more prejudicial to the rights of the defendants than a mere matter of variance.

We sincerely and earnestly ask the Court's indulgence, to briefly review the proceedings in this case, to determine whether the disposition made by this Court in affirming the judgment of the District Court is fair in view of the proceedings in the courts below. We further ask that this Court will review those proceedings from the standpoint of the defendants' counsel, putting itself in their position, in determining whether the final disposition made by this Court is fair and in keeping with judicial impartiality.

As pointed out by this Court the gist of the offenses charged was a wilful attempt or conspiracy to evade taxes in any manner. This is a broad charge. The details of the manner and means of the alleged evasion, ordinarily, must be found in the indictment itself. The substantive counts allege the wilful attempt to evade taxes by a deduction of these commissions. There is no allegation anywhere in these counts as to why these deductions were improper.[1]

The conspiracy count alleged that these deductions were dividends—a distribution of profits to the defendants as stockholders—*and that the defendants rendered no services to the company.* The indictment contains no allegation or suggestion that the commissions were unreasonable compensation for the defendants' services. Such was not the theory of the indictment, as will appear from the gov-

1. These counts do not allege that the defendants "under the guise of paying commissions • • • distributed dividends" as this court twice stated in its opinion and as repeatedly represented to this Court by the government in its brief. For correct analysis of indictment, see our brief, pp. 5-8.

ernment's brief before the Circuit Court of Appeals, where it is stated (page 13).

> "*Again, it must be emphasized that the indictment in the case at bar does not charge that the defendants wilfully attempted to evade and defeat taxes by taking deductions of unreasonable amounts as commission, that is, payment for services;* rather it charges that the defendants wilfully attempted to evade and defeat taxes by claiming as deductions for commissions, amounts which were in fact distributed as dividends and were not intended as compensation for services." (Ital. ours.)

The defendants rested their case without offering any evidence. Just prior to their doing so, in support of their motions for directed verdicts, they took the position that inasmuch as there was an allegation in the indictment that defendants rendered no services for these commissions, and the government's evidence having established that all of the defendants had rendered services, that it was therefore incumbent on the prosecution to at least prove that the deductions were unreasonable compensation for the services so rendered. This was a legal question involving the probative value of the government's evidence as a whole—the same question on which this Court, in its opinion, stated that the evidence was sufficient to go to the jury. What was the government's answer to this position taken by us in the trial court? *The government in effect conceded that its evidence was insufficient to show that these payments were unreasonable when it took the position that this question was not involved in this case.* The position the government took before the trial court was that their evidence as a whole established that these commissions were in their entirety a subterfuge for the distribution of dividends.

The first question Judge Lindley asked the government at the conclusion of our argument was whether or not its evidence showed that the defendants did not earn these

commissions. The government's answer *was that that question was not involved in this case.* We quote:

"The Court: Mr. Hall, let me ask you this question: Does the evidence show that the defendants did not earn any salaries?

"Mr. Hall: *That question is not involved, if the court please.*

"The Court: I wish you would set me right on it.

"Mr. Hall: *The question of what these defendants earned is not involved in this case.*

"The Court: Well, if they earned these commissions they were entitled to them.

"Mr. Hall: The evidence shows, if the court please, on the Government's theory, and it tends to prove it, that these commissions, the charge of commissions was used as a subterfuge to distribute the 70 per cent of the company's net income to the stockholders. Now, I don't care, it doesn't matter under the cases, if it was a subterfuge used for that purpose and there was no agreement for the payment of services or for services rendered to the corporation, whether they performed any services at all or not, if those were dividends they were dividends." (Rec. 459.) (Ital. ours.)

The record is clear and not subject to contradiction that the government position, before the trial court before we rested our case without offering any evidence, was as above outlined.

The record further is clear that the trial court at the time of the argument on the motions for directed verdicts was of the opinion that the government's evidence was insufficient to establish that these payments were unreasonable compensation;[2] that the trial court determined to submit this case to the jury alone on the broad question whether or not the payment of these commissions was but

2. We quote that Court:

"Now, having shown that they rendered some services and that they received these things as commissions, haven't you got to go further and show, in order to create a fraudulent intent, that these commissions received were all out of proportion to the services rendered?" (Rec. 463.)

a subterfuge for the distribution of dividends;[3] that the court did so instruct the jury[4] and that the government fully recognized that this was the theory upon which this case was submitted to the jury.[5]

3. The trial court then stated:

"There is one question in this case which after all, is an ultimate question of facts to be settled and adjudicated through the principles of law and that is whether the sums that were paid in this case to the individual defendants were the distribution of profits of the corporation and therefore not deductible in its income tax return.

"Well, whether they were in effect in good faith in the payment by the corporation for services rendered to the corporation and therefore deductible as ordinary and necessary expenses in the operation of its business under Section 146 of the Revenue Act, I think in that situation the government has certain evidence here which it should have the jury's verdict upon, and whatever my personal views may be, and I admit that I think this is a pretty weak case, I prefer to let it go to the jury and see what develops." (Rec. 465.)

4. This is borne out by further portions of the instructions, which are quoted below:

"So it is a vital question in this case of whether the Consensus Company was entitled to deduct from its income the sums distributed to the defendants as ordinary and necessary expenses of its business. The question is whether it should not rather have reported that those distributions were distributions of the profits of the company to its shareholders rather than the payment of compensation to employes and about that this whole case centers.

"If these sums distributed were distributed as a part of the profits of the corporation, then they should have been accounted for in the income tax report of the Consensus Company as profits and upon that the corporation should have paid a tax, which it did not.

"If, on the other hand, if they were intended to and represented actual bona fide compensation to employes of this corporation in the ordinary operation of its business; in other words, if they were ordinary and necessary expenses of the operation of the business, then they were properly deductible as they were deducted and no tax was due upon them." (Rec. 470.)

5. The government's brief before the Circuit Court of Appeals states, Brief, p. 92:

"Reading the charge as a whole, therefore, it becomes apparent that the court correctly instructed the jury that it was a question of fact—indeed the dominant issue—whether these defendants were stockholders receiving dividends or whether they were employees receiving commissions."

This Court has stated that the trial court also submitted to the jury, by the alleged erroneous instruction, the issue of the reasonableness of the commissions paid. This instruction was only given over defendants' objections after they had rested their case, on the record above referred to and without defendants having offered any evidence, relying upon the government's representations to the trial court that this issue was not involved in this case. It may also fairly be said, that while this instruction did in fact submit the reasonableness of the compensation to the jury, it was not intended for any such purpose. It was given as an abstract proposition of law, namely that in the ordinary income tax case, the government is not bound to prove the entire amount of taxes alleged to have been evaded.[6] Even assuming the trial court intended to give this instruction as the basis for submitting to the jury the question of the reasonableness of the compensation (now claimed by the government for the first time in this Court), the giving of the instruction under the condition of this record was clearly erroneous and prejudicial to the defendants. They had offered no evidence to meet this issue, relying upon the statements of the trial court and the government's position as stated.

At the time our motions for directed verdicts were presented and overruled, it was incumbent upon all defendants to decide whether or not they should offer evidence of a defense. The answer to this question necessarily rested on the indictment, the government's evidence alone and the

6. In the Circuit Court of Appeals, the government nowhere argued that the question of reasonableness of these payments was involved in the case; that their evidence was sufficient for the jury to find that these payments were unreasonable and that, therefore, the instruction in question was proper. The government's position as to this instruction was that numerous courts, including the Seventh Circuit, had held as a matter of law, that the government was not bound to prove that the defendant evaded the exact amount of taxes charged in the indictment. (See Government's Brief, pp. 92-93.)

colloquy between court and counsel which had just taken place in connection with defendants' motions for directed verdicts. What was the theory of the indictment and on what theory did the government claim that its evidence sustained the charges of this indictment? Its theory, as represented to both the trial court and defendants' counsel, was that the payment of these commissions was a mere subterfuge for the distribution of dividends and *the question whether these commissions represented reasonable compensation for services rendered was not involved in this case.* In determining the question whether or not we should offer any defense, we certainly had a right to rely upon the charges of the indictment (the only allegation in the indictment as to why these deductions were improper was that defendants rendered no services); the questions propounded to both sides by the trial court and the position taken by the government in answer to those questions.

In view of this position taken by the government as to this question, there was no reason for the defendants to present evidence of the services rendered by them, to show that they in fact earned these commissions or to show that the payments made them were not unreasonable compensation for their services. There was no reason for any such proof under the theory advanced by the government at that time. Had either the government or the trial court taken the position on which this court based its opinion, that a *prima facie* case had been made out showing that the commissions were unreasonable compensation for the services rendered, it would have been necessary for us to offer a defense. The government not only claimed that this was not the theory of their case but claimed just the opposite namely that this question was not *involved.* Under this state of the record, were the defendants and their counsel bound to anticipate that the government would completely shift its position in this court—a final court of review—and argue that its evidence established that these pay-

ments were unreasonable? Were the defendants and their counsel bound to anticipate that this court, a final court of review, would adopt the argument of the government and in deciding the issues in this case hold that the question of the reasonableness of the compensation paid was the dominant issue in the case and that the government's evidence had established a *prima facie* case on this question? This Court's opinion is necessarily based on its conclusions as above stated.

The government persisted in their position before the trial court in the Circuit Court of Appeals: In its brief before that Court, the government said (page 82):

> "*On the basis of the foregoing, it is respectfully submitted that there is no issue involved in this case regarding the question of whether commissions may be deducted or whether the payments were reasonable.* We cannot repeat too often that there are no questions concerning commissions, because these payments were dividends and were known to be such by the defendants. * * * If the record establishes that these defendants knew they were getting dividends and nevertheless attempted to evade the taxes of the company by charging them as commissions, *then it is palpably immaterial whether they were or were not services or whether the payments did or did not exceed the reasonable value of these services.*" (Italics ours.)

In the oral arguments before that Court, their position still was that these payments were either dividends in their entirety, and therefore improperly deducted, or commissions in their entirety, and therefore a proper deduction—that there could be no middle ground and the question of the reasonableness of the compensation was immaterial. This was entirely inconsistent with their theory of the case before this Court that the payments were unreasonable compensation, the basis upon which this Court made its opinion.

The Circuit Court of Appeals recognized this position

taken by the government. In their opinion that Court said:

> "There was no proof and no effort by the Government to show that the services disclosed constituted the total of those performed and no effort to show the reasonable value of such services." (Rec. 500.)
>
> "*Under the Government's theory, however, it is immaterial and irrelevant as to whether the defendants performed services for which they might have been entitled to compensation or salary. The case was tried and is presented here on that theory. In* other words, the Government argues that conceding the defendants rendered services for which they might have been entitled to compensation, yet the disbursements were received as corporation dividends and were, therefore, unlawful deductions." (Rec. 501.)
>
> "The Government in its brief and in oral argument before this Court asserts that the deductions in question must be treated either as dividends in their entirety, and if so as lawful deductions, or as commissions in their entirety, and therefore properly deducted. In other words, in accordance with this argument there can be no middle ground." (Rec. 502.) (Italics ours.)

There can be no question but that the Circuit Court of Appeals correctly analyzed and stated the position of the government both before the trial court and before that court.[7] This Court has held that the Circuit Court of Appeals erroneously construed the Cohen Grocery case as applicable to the facts here, and, also, this court, in its

7. As conclusive evidence of the position taken by the government in the court below, we have quoted at some length from its brief before that court and the opinion of that court. The opinion of that court further refers to the same position advanced by the government in its oral argument. This oral argument was transcribed and the transcript is in the possession of the Solicitor General. In our brief, page 25, we quoted from this transcript. This transcript will further show that the government before the Circuit Court of Appeals conceded that it had offered no evidence to show that these payments were unreasonable. The Solicitor General has assured us that he will make this transcript available to this court, if it so desires.

opinion, defined the correct principles of law applicable to this case. Under these principles of law, irrespective of the Cohen Grocery case, the Circuit Court of Appeals, in view of the position taken and the concessions made by the government before it, could do nothing else but reverse the judgment of the trial court. **Had the government, before this court, argued that these payments were either proper or improper in their entirety, had the government conceded that they had offered no evidence to show that these payments were unreasonable and had the government argued that the questions of the reasonableness of these payments was not involved in this case, this Court under the very principles of law laid down in its opinion could have done nothing else than to have affirmed the judgment of the Circuit Court of Appeals.**

For the first time, before this court, the government shifted its position and inferentially argued here that there was sufficient evidence from which a jury could infer that these payments were unreasonable. (Govt. Brief, page 33.) We pointed out to this court (Kruse Brief, pages 25-32) that this was a plain shift of position from the government's theory propounded in both of the courts below. We did not develop how unfair such contention was to the defendants when first urged in the final court of review, or how prejudicial such a conclusion by this court would be to the defendants.

The government asked this court to affirm the judgment of the trial court and reverse the judgment of the Circuit Court on a theory which was not only never advanced by the government to the trial court nor propounded by it to the Circuit Court of Appeals, but which theory was in direct contradiction to its theories in both courts below. This court—a court of final review—has adopted this theory. This theory has emerged for the first time here when the defendants cannot possibly offer any proof of any character whatsoever justifying the commissions so

paid to them. Do not the most fundamental principles of fair dealing require that they be afforded that right?

We have been consistent in our position throughout the trial of this case and its review both by this court and the Circuit Court of Appeals.

When this court held,

> "We are convinced that all of this is sufficient to support a finding by the jury that the respondents wilfully attempted to make unreasonable allowances for personal services"

all of our arguments advanced in the previous courts completely fell and became of no avail. We had no opportunity to meet this theory by factual proof in the only place it could have been met—the trial court below—not only because that theory had never been advanced by the government but the government claimed that this question was not even involved in this case.

As heretofore stated, we had a right to rely upon the theory then stated by the government when we determined to offer no defense. Under the opinion of this court, the real and dominant issue was whether or not the defendants earned these commissions. This issue was defined for the first time by this court in its opinion here. It would seem only fair, under these circumstances, that the defendants be afforded the right to meet this issue of fact by offering the defense that they did earn these commissions. The only reason they did not do so in the trial court was because of the fact that the government claimed such issue was not involved in the case.

It may be argued that the defendants and their counsel were bound to comprehend that the government's evidence established a *prima facie* case as to the unreasonableness of the compensation paid. The trial court did not realize this and the government in effect conceded its evidence had no such probative value when it claimed that this ques-

tion was not involved. The government persisted in this position in the Circuit Court of Appeals and again insisted that this issue was not involved in the case. The Circuit Court of Appeals reversed the case in reliance upon the position so taken by the government. In view of these circumstances, it would indeed be unfair, to say to the least, to attribute to defendants' counsel the ability to foresee a disposition of this case by the highest court of review upon a theory which the government at the time of trial definitely stated was not involved in the case, and so argued to the Circuit Court of Appeals.

Conclusion.

The administration of criminal jurisprudence is not a catch-as-catch-can game. It must afford to every defendant a full opportunity to present a defense upon the merits of the case as set forth in the indictment and propounded by government counsel. The law favors a trial on the merits. We have no complaint whatsoever to offer to the principles laid down by this court in its opinion. We do, however, earnestly and sincerely contend that the only fair treatment that can be afforded to these defendants, in view of that opinion, is to remand the case to the trial court for a retrial.

Respectfully submitted,

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JOSEPH A. STRUETT,
WARREN CANADAY,
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P. 8

SUPREME COURT OF THE UNITED STATES.

Nos. 54, 55, and 56.—October Term, 1941.

54	The United States of America, Petitioner, *vs.* James M. Ragen,	On Writs of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.
55	The United States of America, Petitioner, *vs.* Arnold W. Kruse,	
56	The United States of America, Petitioner, *vs.* Lester A. Kruse.	

[January 5, 1942.]

Mr. Justice Black delivered the opinion of the Court.

Section 145 of the Revenue Act of 1932 provides that "any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof, shall, in addition to other penalties provided by law, be guilty of a felony . . . ." 47 Stat. 217. (There are identical provisions in the Revenue Acts of 1934 and 1936. 48 Stat. 725; 49 Stat. 1703.) Petitioners were indicted, tried, and convicted in the District Court for conspiracy to violate, and for violation of, this provision. The Circuit Court of Appeals, one judge dissenting, reversed. *United States* v. *Molasky*, 118 F. 2d 128. Because questions of importance in the enforcement of this criminal statute and the administration of the revenue laws were raised, we granted certiorari. 313 U. S. 557.

In computing net corporate income subject to tax, a deduction is permitted for "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered . . . ." Sec. 23(a), Revenue Acts of 1932, 1934, and 1936. 47 Stat. 179; 48 Stat. 688; 49 Stat. 1658. "Dividends" distributed from net corporate profits are not allowable deductions. But "commissions", if incurred as necessary business expenses and as a reasonable allow-

ance for personal services actually rendered, are deductible from gross income. The larger the allowable deduction the smaller are the net taxable income and the tax imposed. The first four counts of the indictment set out attempts by the defendants to evade income taxes of the Consensus Publishing Company for the years 1933 to 1936, through a fraudulent scheme whereby, under the guise of paying commissions which were deducted from gross income, the corporation distributed dividends deduction of which the statute does not permit. The fifth count sets out a conspiracy to accomplish similar results for the years 1929 to 1936.

After an examination of the evidence in the record including numerous exhibits, we are satisfied that the jury could justifiably have found the following facts to be true.

The Consensus Publishing Company, an Illinois corporation, was organized in 1929 to carry on the business of preparing "run-down" sheets, daily bulletins containing information on horse racing, and selling them to bookmakers. The original stock ownership was distributed among Arnold Kruse (20 shares), James Ragen, Sr. (20 shares), William Molasky (30 shares), and Cecelia Investment Company (30 shares), a holding company controlled by Moses Annenberg, the dominant figure in several other corporations which were engaged in enterprises connected with betting on horse races. Kruse and Ragen were executives in other Annenberg companies. Molasky alone lived in St. Louis, where Consensus conducted its principal business operations, but he delegated to one Gordon Brooks, an employee of another corporation owned by Molasky, the job of collecting receipts, preparing records and reports, and supervising printing for Consensus, work which took Brooks an hour and a half a day on the average except for the one day each week when the preparation of operating reports for the Chicago office required about three hours.

For several years Consensus made a weekly distribution of money to its shareholders in direct proportion to their holdings. In the period covered by the indictment, only the 30% of the distribution going to Cecelia Investment Company was treated as dividends in Consensus' tax returns. The remaining 70%, although referred to in some of the corporation's confidential weekly reports to stockholders during the period as "dividends", was nevertheless in its income tax return deducted from gross income as "commissions." The deductions thus claimed were $10,761 in 1929, $62,961 in 1930, $64,791 in 1931, $37,255 in 1932, $54,538 in 1933,

$60,172 in 1934, $76,714 in 1935, and $119,756 in 1936. The book-keeping system under which 70% of the funds remaining after payment of expenses was charged as commissions was set up in 1929 in accordance with instructions from Arnold Kruse.

In 1934, Kruse, having learned of a decision of the Board of Tax Appeals that distributions of profits as commissions would not be allowed as a deductible expense if made in accordance with stockholdings, set in motion a series of transactions retroactively modifying the relationship between Consensus and its stockholders. He directed an employee to destroy the original stock book of the company, issue new stock certificates bearing the date of incorporation (September 18, 1929), and then immediately to cancel the new certificates and issue a single certificate for one hundred shares to the Cecelia Investment Company. In 1935 or 1936, Kruse ordered the drawing up of written yearly contracts of employment for the several years from 1930 on between Consensus and the individuals to whom "commission" payments had since the inception of the company been made. In each contract, the compensation was to correspond identically with the amount that had already actually been paid.

Except for delays in destroying the original stock book and the original stock certificates, this plan was promptly carried out. Moreover, corporate minutes were drawn up, appropriately back dated, which set out the stock "issue" and the employment contracts as if they were actual events contemporaneous with the false dates of recording.

Among the back dated contracts were several between Consensus and the respondent Lester Kruse, son of Arnold. These together with a back dated assignment by Arnold to Lester of his "contract of employment" with Consensus were to afford ostensible documentation of a shift to Lester, after March, 1933, of the share that had formerly gone to Arnold.[1] Similarly, after 1931, Consensus paid the share that had formerly gone to Ragen to Ragen's son. Here, too, a set of back dated papers documenting the shift was fabricated. After their sons became the nominal recipients of commissions, Kruse and Ragen continued to be connected with the affairs of Consensus. Kruse, for example, directed the creation of the spurious papers and records already described, and Ragen

[1] Or to his wife. From August, 1932, to March, 1933, Consensus distributed 20% of its earnings to Mrs. Arnold Kruse. No explanation is apparent in the record.

from time to time at least until 1935 signed "commission" checks of Consensus which were paid in regular course.[2]

If, from the foregoing and other supporting evidence in the record, the jury could have found that any one of the defendants had, with the intentional cooperation of the others, received "commissions" without rendering any services whatsoever, it would have been possible for the trial judge to have submitted the case to the jury without calling upon it to decide any questions of reasonableness of compensation for services actually rendered. If, however, each defendant had performed some service for the corporation, the jury would have had to consider whether or not the "commissions" had intentionally been made excessive so that a portion of payments made in the guise of meeting expenses actually constituted a distribution of dividends. There was evidence which, if believed, tended to establish that each defendant had performed some service, although of an irregular and undefined nature. Hence, it seems to us entirely proper for the trial judge to have submitted the case to the jury with a charge not necessarily calling for a determination of whether all or none of the "commissions" paid to each defendant were dividends, but permitting a determination of whether the "commissions" were intentionally made to *include* substantial amounts which should have been treated as dividends. Upon such a charge,[3] the jury found Arnold Kruse

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[2] Because of this and other circumstances showing Ragen's continued participation in the affairs of Consensus, we conclude that the argument, separately made on his behalf, that there was insufficient evidence to establish his connection with any scheme to evade taxes, is without merit.

[3] The crucial portions of the District Judge's charge to the jury are as follows:

"If these sums distributed were distributed as a part of the profits of the corporation, then they should have been accounted for in the income tax report of the Consensus Company as profits and upon that the corporation should have paid a tax, which it did not.

"If, on the other hand, they were intended to and represented actual bona fide compensation to employes of this corporation in the ordinary operation of its business; in other words, if they were ordinary and necessary expenses of the operation of the business, then they were properly deductible as they were deducted and no tax was due upon them.

. . . . . .

We are concerned only with the question of whether these men have entered into a conspiracy, into a scheme whereby as a result this corporation, the Consensus Company, under the guise of commissions, distributed to its shareholders sums that actually represented a division of profits.

and Ragen guilty on all five counts, and Lester Kruse guilty on counts four and five.[4]

In the charge as given, the Circuit Court of Appeals found reversible error. The gist of the court's argument is contained in the following excerpt from the opinion:

"We have reached the conclusion that where a statute permits a reasonable deduction for services, a criminal prosecution can not be maintained by proof other than that such services were not rendered. It is not sufficient to allege or prove that a deduction claimed for services is unlawful because the amount charged is unreasonable. Such a charge would leave to the trier of the facts the responsibility for fixing the standard by which a defendant's guilt would be determined. The standard would vary according to the views of different courts and juries. Such a theory would be violative of the defendant's constitutional rights, and void. United States *v.* L. Cohen Grocery Co., 255 U. S. 81 . . .; International Harvester Co. *v.* Kentucky, 234 U. S. 216, 221 . . .; Collins *v.* Kentucky, 234 U. S. 634, 638 . . ."[5]

Determination of allowable deductions by reference to a standard of "reasonableness" is not unusual under federal income tax laws. For example, the deductions allowed for depreciation and obsolescence, for bad debts, and for ordinary and necessary business expenses (other than compensation for services) are designated in the Internal Revenue Code as "reasonable." 53 Stat. 1, Secs. 23(l), 23(k)(1), 23(a)(1). If, as the opinion below suggests, the only question that can properly be submitted to the jury is whether the *entire* deduction is fabricated, an unconscionable taxpayer can immunize himself from the criminal sanctions for tax evasion by the simplest of expedients. He need only find a legitimate item of deduction and then pad it as much as his purpose requires. By

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"If these defendants had that kind of plan and carried it out, if they wilfully and intentionally entered into such an arrangement, there wouldn't be any question of their guilt.

. . . . . .

It is not necessary for the government under this indictment to prove that all of the sums so distributed to these defendants were profits. It is not necessary that the government prove all of the figures precisely as they are charged in the indictment. It is sufficient if you find beyond a reasonable doubt that the defendants intentionally diverted profits of this concern, in the amount charged in the indictment or substantial parts thereof, diverted them from the form of profits and received them in the form of commission."

[4] Molasky, James Ragen, Jr., and the Consensus Publishing Company were also found guilty. The government has not sought review of the Circuit Court of Appeals' reversal of the conviction of Molasky and James Ragen, Jr., which involved additional issues of no relevance to the respondents here. The corporation did not take an appeal from the judgment of the District Court.

[5] United States *v.* Molasky, *supra*, 139.

transforming the question "Should any deduction have been made?" into "Was the deduction made in excess of a reasonable allowance?" he can, if the theory accepted below be correct, largely destroy the deterrent effect of a penal statute passed by Congress.

We have concluded, however, that the ground of decision below is untenable. The mere fact that a penal statute is so framed as to require a jury upon occasion to determine a question of reasonableness is not sufficient to make it too vague to afford a practical guide to permissible conduct. Cf. *Nash* v. *United States*, 229 U. S. 373. The cases cited by the Court of Appeals affirm no such proposition. In the *Cohen Grocery* case, this Court held a conviction under Section 4 of the Lever Act, 41 Stat. 297, 298, unconstitutional because the statute left open "the widest conceivable inquiry, the scope of which no one can foresee and the result of which no one can foreshadow or adequately guard against," and because an "attempt to enforce the section would be the exact equivalent of an effort to carry out a statute which in terms merely penalized and punished all acts detrimental to the public interest when unjust and unreasonable in the estimate of the court and jury." *United States* v. *Cohen Grocery Co.*, *supra*, 89. In the *International Harvester* case, this Court expressed the view that assurance that the state statute there in issue was complied with called for "gifts that mankind does not possess." *International Harvester Co.* v. *Kentucky*, *supra*, 224. And in the *Collins* case, the same statute was said to call for a determination of conduct "not according to the actualities of life, or by reference to knowable criteria, but by speculating upon imaginary conditions." *Collins* v. *Kentucky*, *supra*, 638.

No such unworkable standards are involved here. Section 145 of the Revenue Act of 1932 standing alone is not vague nor does it delegates policy making powers to either court or jury. It declares that "any person who willfully attempts in any manner to evade or defeat any tax imposed" by the act "shall . . . be guilty of a felony" and specifies penalties in addition to those otherwise provided by law. That such acts of bad faith are not beyond the ready comprehension either of persons affected by the act or of juries called upon to determine violations need not be elaborated. Nor does the particular mode of evasion here alleged, intentional deduction of dividends in the guise of compensation for personal services, so transform the nature of the offense as to make the actors less aware that they are committing it or juries less competent to detect it. The statutory specification of permissible deduction here

in question is of long standing. For years thousands of corporations have filed income tax returns in accordance with the direction to deduct "a reasonable allowance for salaries or other compensation for personal service actually rendered," and there has not been any apparent general confusion bespeaking inadequate statutory guidance. A finding of unconstitutional uncertainty in this section of the act as applied here would be a negation of experience and common sense.

On no construction can the statutory provisions here involved become a trap for those who act in good faith. A mind intent upon willful evasion is inconsistent with surprised innocence. Cf. *Gorin* v. *United States*, 312 U. S. 19; *Hygrade Provision Co.* v. *Sherman*, 266 U. S. 497; *Omachevarria* v. *Idaho*, 246 U. S. 343. And the charge given by the trial court amply instructed the jury that scienter is an essential element of the offense.

We conclude that it was not error to submit to the jury the question of whether or not the respondents attempted to make unreasonable allowances for personal services. The respondents, however, raise a further objection going not to the propriety of such a submission as a matter of law, but to the insufficiency of the evidence upon which the jury could have found an answer to the question submitted. They contend that the record discloses that the recipients of commissions performed some services; that the record fails to show that the services disclosed were the only services rendered; that there was no direct testimony as to the total amount of services rendered or the reasonable value thereof; and that, therefore, the jury had no rational basis upon which to conclude that the sums deducted as "commissions" were more than a reasonable allowance for compensation for the services rendered. We must reject this contention.

The business conducted by Consensus, a business which, according to the testimony of a person who was in immediate charge of its major operations, normally required only an hour and a half daily of managerial supervision, would hardly seem to call for additional executive services worth what Consensus paid in "commissions." The same witness testified that he had never seen some of the recipients of "commissions", and that his only contact with one of them was two telephone conversations. This testimony, too, belies participation by the respondents in the business activities of Consensus to a degree justifying payment of the high "commissions"—equal on the average to about half of gross revenues and amounting

each year to several times all other wages and salaries[6]—as a *quid pro quo* for their services. Moreover, there is the additional circumstance, damaging to the respondents' contention, that year in and year out, 30% of earnings after deduction of expenses was paid to the Cecelia Investment Company as dividends, and 70% to the respondents or other individuals as "commissions." This uniformity in the computation of "compensation" is difficult to reconcile with the variations in extent and kind of personal services which one would expect to find in accounts reflecting bona fide allowances for personal services. Further, there is the circumstance that the "commission" payments were always in proportion to original stock holdings. And darkening the whole picture is the atmosphere of purposeful concealment evinced by the destruction of some important corporate papers and the fabrication of others. We are convinced that all of this is sufficient to support a finding by the jury that the respondents willfully attempted to make unreasonable allowances for personal services.

The respondents also urge that there was a fatal variance between the indictment and the proof in that the indictment alleges that the commission payments were actually dividends in their entirety whereas the evidence indicates that some services were performed. The fifth count of the indictment does refer to "all of the moneys . . . paid . . . by virtue of the . . . so-called 'Employment Contracts'" as "in truth and in fact, distributions of profits and dividends." But the gravamen of the charge is distribution of dividends in the guise of commissions, and the respondents cannot fairly claim that they were not adequately apprised of the nature of the offense. Any variance which existed, at most a matter of the extent of the alleged tax evasion, involves no elements of surprise prejudicial to the respondents' efforts to prepare their defense. Cf. *Berger* v. *United States*, 295 U. S. 78; *Bennett* v. *United States*, 227 U. S. 333.

The respondents have made further contentions which we conclude after consideration are without merit.

The judgment of the Circuit Court of Appeals is reversed and that of the District Court affirmed.

It is so ordered.

Mr. Justice ROBERTS, Mr. Justice MURPHY, and Mr. Justice JACKSON took no part in the consideration or decision of this case.

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[6] In 1936, for example, "commissions" amounted to $119,756 as compared with $8,816 paid out for other wages and salaries.